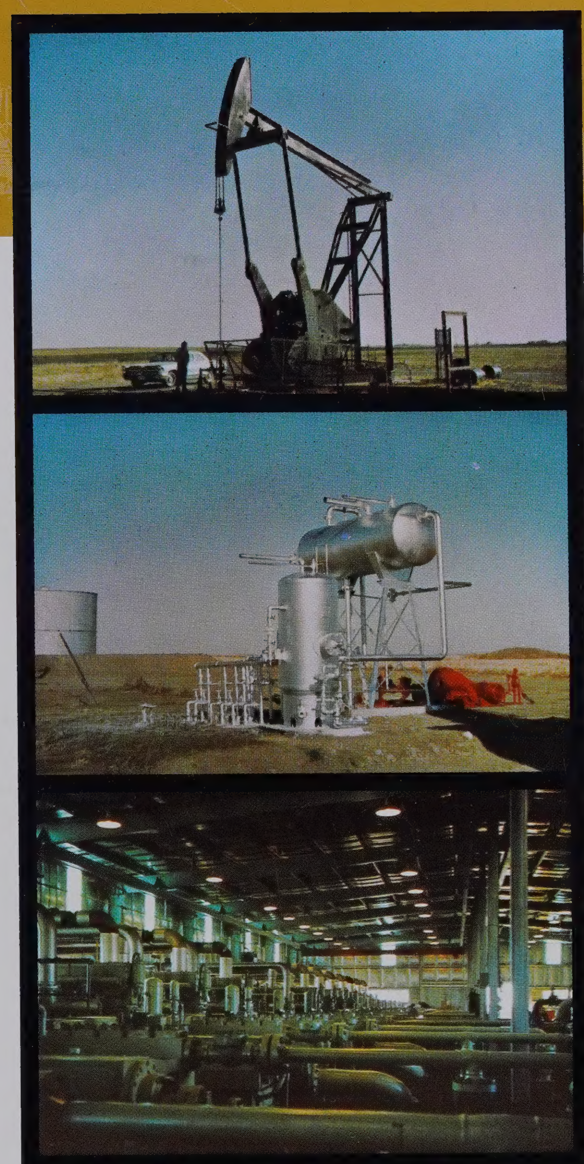
CENTRAL-DEL RIO OILS LIMITED



1964 ANNUAL REPORT

CENTRAL-DEL RIO OILS LIMITED

EIGHTEENTH ANNUAL REPORT FOR THE YEAR ENDED DECEMBER 31, 1964

Cover

Top: Long stroke, high volume pump jack, of a type larger than most used in Canada, pumping one of the oil wells in the Weyburn Unit, Saskatchewan.

Centre: One of several installations in the Weyburn Unit for measuring individual well producing rates and separating gas from oil and water prior to their transmission to the central treating and water injection plant.

Bottom: Interior of Weyburn Unit central plant, showing a bank of engines and high pressure pumps used to inject water into the producing formation for greater oil recovery.

Photos by J. V. Sinclair, Central-Del Rio geologist based at Weyburn.

Annual Meeting

The Annual Meeting of Shareholders of the Company will be held at the Palliser Hotel, Calgary, Alberta, at 10 a.m. on Wednesday, April 14, 1965. Notice of meeting and proxy forms have been mailed to all registered shareholders.

Financial and Operating Summary

	For the Years ended December 31 1964	1963
FINANCIAL		
INCOME	$7,748,949	$7,662,690
NET PROFIT before depreciation, amortization and income taxes	$4,935,775	$5,273,618
NET PROFIT before income taxes	$2,414,300	$2,810,303
INCOME TAXES	$ 257,009	$ 536,951
NET PROFIT for the year	$2,157,291	$2,273,352
CASH DIVIDEND paid	$ 977,282	$ 648,504
WORKING CAPITAL — as of December 31	$4,582,886	$4,877,119
— Decrease during the year	$ 294,233	$1,476,184
OPERATING		
— Oil sold for company account *(bbls.)*	2,855,465	3,107,815
— Average daily sales *(bbls.)*	7,802	8,515

DIRECTORS' REPORT TO THE SHAREHOLDERS

The year 1964 was a busy and successful one for Central-Del Rio Oils Limited. Exploration and operating activities reached new high levels and, despite a temporary decline in output of oil from your Company's major source of production at Weyburn, Saskatchewan, very satisfactory financial results were obtained, as shown by the comparative summary on the facing page and the audited Consolidated Financial Statements reproduced on pages 7 to 10 following.

Total income was $7,748,949, exceeding the record high of the previous year, although revenue from oil sales after payment of royalties was $301,978 less than in 1963. The year's increase of $388,237 in income from other sources more than offset reduced production income. Revenue from investments and a non-recurring profit from the sale of a drilling rig contributed to this improvement in other income, as did the first full year's fees for operating the Weyburn Unit.

Expenses attributable to operation of the Weyburn Unit were considerably higher in 1964, both in the field and as a part of administrative and general expense, also reflecting the full year's operations; and lease rentals were up significantly, due to large additions to the Company's acreage holdings. Mainly for these reasons, total expenses in the year under review amounted to $424,102 more than in 1963.

Under the combined influence of these changes, Central-Del Rio in 1964 generated a $4,935,775 net profit before provision for depreciation, amortization and income taxes. This cash profit, which may be compared with the $5,273,618 realized in 1963, is very gratifying, in view of the pause in rate of production.

Non-cash write-offs for depreciation of plant and equipment and amortization of lands, leases and well costs totalled $2,521,475 in 1964, moderately more than the comparative figure of $2,463,315 for the previous year; and provision for income taxes was down substantially, from $536,951 to $257,009.

Net profit for the year, after royalties, expenses, write-offs and provision for income taxes, was $2,157,291, second only in the Company's history to the $2,273,352 achieved in 1963. Net profit per share was 33¢.

For several years your Management has been of the opinion, shared by many people both inside and outside the oil industry, that published oil company financial statements are, broadly speaking, unnecessarily difficult for a large segment of the investing public to understand. Accordingly, more than a year ago, our accounting staff was assigned the task of carrying out a detailed and critical analysis of oil industry accounting policies and recommending for adoption by the Company any changes in its policy, consistent with generally accepted accounting practice, which would result in better and more informative presentation. This study ultimately focused on one major point of difference between the practices which have been followed historically by many oil companies, on the one hand, and by industrial enterprises in general, on the other. Companies outside the oil

industry have adhered closely to the concept of full cost accounting; but oil companies have departed from that concept in one important respect, by deducting from cash profit, in lump sums, the widely varying costs of lands abandoned, dry holes drilled and geological and geophysical work carried out during each year. That practice often produces inflation of net profit in a year of poor revenues, when land abandonments have been minimal or little expenditure has been made on exploration in search of new reserves. If both of these conditions apply, the result may be quite misleading. Conversely, in a year of good revenues, with substantial land abandonments or large expenditures on exploration, or both, net profit may be unrealistically low. Therefore, the net profit figures in many oil company financial statements have little meaning.

"Oil is where you find it"; and only a small percentage of the widespread acreage holdings of any company engaged in the search will turn out to be productive. All of the costs of this land and the drilling and other exploratory work done on it must be recovered out of the relatively few tracts from which production is obtained. It is only sensible, therefore, in the interest of lucid financial reporting, to capitalize these costs initially and then, over the years, charge a portion of them to each barrel of oil or other unit of production as it is recovered and sold, instead of arbitrarily writing them off in lump sums. This change in accounting policy, which has recently been made by several companies prominent in the industry, has been recommended to and accepted by your Management and Board of Directors, and the Company's accounts have been retroactively adjusted accordingly, on a comparative basis. We believe that you, the Shareholders, will appreciate the change, as will many other interested people who have long wished for greater clarity in oil industry financial reporting.

Working capital dropped from $4,877,119 at the end of 1963 to $3,632,293 at mid-1964 and then rose to $4,582,886 at December 31, 1964, in response to heavy capital expenditures and reduced production income in the first half of the year, followed by decreased capital expenditures and increased production income in the last half. Revenue from production continues to increase, and the major portion of the large cost of capital facilities and equipment for the Weyburn Unit is now behind us. Expenditures during the year on plant and equipment amounted to $830,787, and our outlays for lands, drilling and exploration totalled $3,491,235, all from internally generated funds. An extra dividend of 5¢ per share was added to the 10¢ per share which has been paid in each year since 1960, bringing the total dividend payment in 1964 to $977,282, as compared with $648,504 in 1963.

Oil sold for Central-Del Rio's account in 1964 aggregated 2,855,465 barrels, for a daily average of 7,802 barrels. Sales in the preceding twelve-month period were 3,107,815 barrels in total, and averaged 8,515 barrels per day. While production from other sources was increased by a daily average of nearly 200 barrels for 1964, output from the Weyburn Unit, as explained in the Interim Report to Shareholders for the first half of the year, declined temporarily, due to the

conversion to water injection wells of 121 of the 550 producing oil wells included in the Unit at the time of its formation. These wells were converted in order to implement a pressure maintenance scheme which, by replacing the many millions of barrels of oil produced from the reservoir prior to unitization and the quantities to be produced in future, will greatly increase daily and total ultimate output of oil from the unitized zone. In July, 1963, the first month of unitized operations, your Company's average production of Weyburn Unit crude was 7,220 barrels daily. Following conversion of the 121 wells and commencement of water injection, production dropped in August, 1964 to an average of 6,046 barrels per day, and it was not until January, 1965 that it regained the July, 1963 level under the impetus of the flood. Substantial monthly increases in production are now being obtained; and the Unit has been enlarged, since the close of the year under review, by the inclusion of 58 additional wells.

Central-Del Rio's operations in 1964 included the drilling or participation in the drilling of 47 wells, of which 13 are producing oil and 2 are gas wells. Pending further evaluation, 2 wells which may have commercial possibilities were suspended. Abandoned wells totalled 28, and target depth had not been reached in 2 wells at the year-end.

Your Company's gross land holdings were increased from 3,039,755 acres to 3,716,949 acres during the year. Net land holdings rose from 1,224,349 acres to 1,762,990 acres. Land holdings under mineral titles remained at 793,949 gross acres and 92,560 net acres.

Although no large oil or gas discovery was made on Central-Del Rio's holdings in 1964, your Company acquired during the year, both by purchase and by farmout drilling, several significant blocks of geologically attractive acreage. In addition, a great deal of valuable information about our lands was gained from exploratory work, and the Company's prospects of finding important new reserves on its now extensive landspread are very good. One example of those prospects is afforded by a recent development adjacent to our holdings. Early in February, 1965, the Banff Aquitaine Rainbow West 7-32 well obtained an estimated 1200 to 3600 barrel per day flow of 38 gravity oil from the middle Devonian. The well is located in the Zama Lake area of Alberta, one and one-half miles to the east of a 92,160-acre petroleum and natural gas reservation owned by your Company and four miles to the south of other large land blocks in which Central-Del Rio holds a 50% interest. It will be impossible for several months to determine whether or to what extent this discovery may benefit Central-Del Rio, because the area is not yet accessible in summer, but it seems likely that it will lead to some interesting exploratory work on our holdings next winter.

Legislative and regulatory changes made in 1964 have given us added incentive to explore in Alberta and Saskatchewan. The Alberta oil production prorationing system has been altered in several respects, with the principal result

that fields with large reserves will produce a greater share of the Province's total output than they have in the past. Your Company's land acquisition and exploratory programs in Alberta have been and will continue to be concentrated mainly in areas where reserves, if discovered, are likely to be large. Saskatchewan has made an extensive overhaul of its mineral resources legislation. Most significantly, the rewards to be gained by discovery of reserves in formations below the Mississippian are enhanced by changes permitting the selection by the drilling party of more acreage than could previously be obtained out of Crown exploration permits, relaxing restrictions on choice of the lands to be leased out of drilling reservations and providing for royalty-free periods and extension of time for rental refunds in certain instances. It is expected that this will stimulate interest in deep drilling, very little of which has been done in Saskatchewan. An increase in that type of activity will be of benefit to your Company, which has large landholdings in the Province.

Central-Del Rio made good progress in 1964 and its prospects for the future were never better than they are now. We express our thanks and congratulations to all members of our excellent staff, whose wholehearted efforts have contributed so much to the Company's continued growth and success.

On behalf of the Board of Directors,

President.

Calgary, Alberta
March 5, 1965

CENTRAL-DEL RIO OILS LIMITED

Consolidated Statement of Profit and Loss

	For the Years ended December 31	
Income:	**1964**	**1963***
Crude oil sales less royalties paid	$6,527,647	$6,829,625
Other — fees, investment and miscellaneous	1,221,302	833,065
	7,748,949	7,662,690
Expenses:		
Production and field	1,432,233	1,301,749
Administrative and general	792,393	680,558
Lease rentals	588,548	406,765
	2,813,174	2,389,072
Net profit before provision for the following:	4,935,775	5,273,618
Depreciation of plant and equipment	458,353	302,470
Amortization of lands, leases and well costs (Note 1)	2,063,122	2,160,845
	2,521,475	2,463,315
Net profit before providing for taxes on income	2,414,300	2,810,303
Provision for taxes on income (Note 4)	257,009	536,951
Net profit for year	$2,157,291	$2,273,352

Consolidated Statement of Surplus

Balance at beginning of year	$6,103,542	$2,322,182
Add:		
Adjustment arising from change in accounting policy with respect to oil and gas properties (Note 1)	—	2,156,512
Net profit for year	2,157,291	2,273,352
	8,260,833	6,752,046
Less cash dividend of 15¢ per share (1963 — 10¢ per share)	977,282	648,504
Balance at end of year	$7,283,551	$6,103,542

* The 1963 figures have been revised to give effect to the change in accounting policy referred to in Note 1.

The accompanying notes to consolidated financial statements form an integral part of these statements.

CONSOLIDATED

ASSETS

	As at December 31, 1964	As at December 31, 1963*
Current Assets:		
Cash	$ 441,219	$ 354,542
Accounts receivable	1,395,019	1,918,929
Short term investments	2,607,563	4,364,932
Marketable securities, at cost (quoted market value 1964—$1,617,078; 1963—$1,314,750)	1,283,940	1,283,940
Inventory of materials and supplies, at cost	81,224	40,351
Prepaid expenses	19,700	2,715
Total Current Assets	5,828,665	7,965,409
Loans, Agreement Receivable and Deposits	48,432	86,307
Fixed Assets, at cost: (Note 1)		
Plant and equipment	6,435,620	6,126,570
Lands, leases and well costs	35,554,777	32,521,993
	41,990,397	38,648,563
Less accumulated depreciation and amortization	13,064,807	11,379,945
	28,925,590	27,268,618
Investment in Affiliated Company, at cost:		
Minerals Ltd.	688,306	688,306
Other Investments, at cost	135,914	135,739
	$35,626,907	$36,144,379

* The 1963 figures have been revised to give effect·

The accompanying notes to consolidated financi

The Auditors' Report

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BALANCE SHEET

LIABILITIES

Current Liabilities:	As at December 31, 1964	As at December 31, 1963*
Accounts payable	$ 1,006,362	$ 2,850,437
Accrued wages and holiday pay	16,340	15,882
Royalties payable	114,218	114,356
Income taxes payable	108,859	107,615
Total Current Liabilities	1,245,779	3,088,290

SHAREHOLDERS' INVESTMENT

Capital Stock:		
Authorized: 10,000,000 shares without nominal or par value		
Issued and fully paid: (Note 3) 6,515,215 shares (December 31, 1963, 6,487,084 shares)	27,097,577	26,952,547
Surplus, as per Consolidated Statement of Surplus	7,283,551	6,103,542
	$35,626,907	$36,144,379

Approved on behalf of the Board:

M. McQueen Director

J. Hardy Director

e change in accounting policy referred to in Note 1.

atements form an integral part of this statement.

tached to this Balance Sheet.

CENTRAL-DEL RIO OILS LIMITED

Notes To Consolidated Financial Statements

AS AT DECEMBER 31, 1964

NOTE 1 - **Change in Accounting Policy**

The Companies have effected a change in accounting policy with respect to oil and gas properties. Acquisition costs of all lands and leases, together with all exploration and drilling costs are capitalized. These costs are then amortized on a unit of production basis, using separate cost groupings for Canada, the United States of America, and elsewhere.

Prior to 1964, costs of lands, leases and productive drilling were capitalized and amortized on a unit of production basis. Unproductive drilling costs and exploration costs were charged to expense as incurred. Costs of abandoned properties were written off at the time of abandonment.

The change in policy resulted in a retroactive adjustment of $2,274,827 in respect of prior years. Of this amount, $2,156,512 representing amounts applicable to 1962 and prior years, is shown as an adjustment in the statement of surplus for 1963, as revised. The balance of $118,315 representing the amount applicable to 1963 is incorporated in the statement of profit and loss for 1963, as revised. The change in policy also resulted in the net profit for 1964 being $2,157,291 instead of $532,708, and in the net profit for 1963 being $2,273,352 instead of $2,155,037. The 1963 comparative statements have been revised to give effect to the change in accounting policy.

No change in the provision for taxes on income was required as a result of the change in accounting policy.

NOTE 2 - **Share Options Outstanding**

The following share options are outstanding as at December 31, 1964:

8,750	shares at $5.50 to employees before January 1, 1967
115,000	shares at $8.25 to employees before February 20, 1967
3,000	shares at $7.50 to employees before May 1, 1967
6,079	shares at $7.75 to employees before May 1, 1967
6,480	shares at $7.50 to employees before April 1, 1968
4,294	shares at $7.50 to employees before July 1, 1968
6,910	shares at $7.50 to employees before March 1, 1969
73,495	shares at $7.50 to employees before November 1, 1969
10,000	shares at $7.25 to an employee before December 1, 1969

NOTE 3 - **Capital Stock Issued**

During the year 28,131 shares of the capital stock of the Company were issued under share option plans for a cash consideration of $145,030.

NOTE 4 - **Income Taxes**

For purposes of determining income taxes, the Companies claim the maximum allowable deductions for development, well costs, depletion and depreciation, which deductions are in excess of those charged in the accounts.

NOTE 5 - **Executive Remuneration and Legal Fees**

The total amount deducted in the consolidated statement of profit and loss in respect of salaries and other remuneration paid to counsel, solicitors and executive officers including all salaried directors was $219,885 for the year ended December 31, 1964 ($188,928 for 1963.)

Auditors' Report To The Shareholders

We have examined the consolidated balance sheet of Central-Del Rio Oils Limited as at December 31, 1964 and the consolidated statements of profit and loss and surplus for the year ended on that date and have obtained all the information and explanations we have required. Our examination included a general review of the accounting procedures and such tests of accounting records and other supporting evidence as we considered necessary in the circumstances.

In our opinion and according to the best of our information and the explanations given to us and as shown by the books of the Companies, the accompanying consolidated balance sheet and consolidated statements of profit and loss and surplus are properly drawn up so as to exhibit a true and correct view of the state of the affairs of the Company and its wholly-owned subsidiaries as at December 31, 1964 and the results of their operations for the year ended on that date, in accordance with generally accepted accounting principles applied on a basis consistent (except for the change in accounting policy with respect to oil and gas properties as referred to in Note 1, with which change we concur) with that of the preceding year.

Calgary, Alberta
February 25, 1965

PRICE WATERHOUSE & CO.
Chartered Accountants

CENTRAL-DEL RIO OILS LIMITED

Consolidated Statement of Source and Application of Funds

FOR THE YEAR ENDED DECEMBER 31, 1964

Source of Funds:		
Net profit for the year ended December 31, 1964 before deduction for depreciation, amortization and income taxes	$4,935,775	
Less provision for taxes on income	257,009	$4,678,766
Proceeds from sale of capital stock		145,030
Reduction in loans, agreement receivable and deposits		40,426
Sale of surplus production equipment		141,024
Decrease in working capital		294,233
		$5,299,479
Application of Funds:		
Plant and equipment		$ 830,787
Lands, leases and well costs		3,491,235
Payment of dividend		977,282
Investments		175
		$5,299,479

Synopsis of Accounting Practice

Acquisition costs of all lands and leases together with all costs of drilling and exploration are capitalized. Costs are amortized on a unit of production basis using separate groupings for Canada, the United States of America and elsewhere. The amortization is the percentage of estimated remaining recoverable drilled proven reserves which has been produced during the year.

Lease rentals are charged against income as incurred.

Costs of plant and equipment are depreciated at rates calculated to write off the costs over periods not exceeding the useful life of the assets.

CENTRAL-DEL RIO OILS LIMITED

Head Office: 224 - 9th Avenue S.W., Calgary, Alberta

DIRECTORS	G. H. ALLEN, Q.C. R. C. CARLILE H. G. GAMMELL JOHN F. HARDY NEIL MCQUEEN D. L. REDMAN J. C. ROSS G. J. VAN DEN BERG DONALD WINSTON
OFFICERS	NEIL MCQUEEN, *President* JOHN F. HARDY, *Executive Vice-President and General Manager* D. L. REDMAN, *Vice-President — Operations* R. W. BURNS, *Vice-President — Exploration* C. M. MACINNES, *Secretary* V. B. WATSON, *Treasurer* A. BARRY BEAVEN, *Assistant Secretary* A. V. SPROULE, *Administrative Assistant*
REGISTRAR AND TRANSFER AGENT	GUARANTY TRUST COMPANY OF CANADA Calgary - Montreal - Toronto - Vancouver
BANKERS	THE ROYAL BANK OF CANADA
COUNSEL	ALLEN, MACKIMMIE, MATTHEWS, WOOD, PHILLIPS & SMITH Barristers and Solicitors - Calgary, Alberta
AUDITORS	PRICE WATERHOUSE & CO. Chartered Accountants - Calgary, Alberta

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